IN THE UNITED STATES DISTRICT COURT
FOR THE EASTERN DISTRICT OF PENNSYLVANIA

MEDMARC CASUALTY INSURANCE COMPANY,	:	
Plaintiff,	:	CIVIL ACTION
v.	:	NO. 01-cv-2394
ARROW INTERNATIONAL, INC.,	:	
Defendant.	:	

MEMORANDUM

BUCKWALTER, J. July 29, 2002

Presently before the Court are Plaintiff Medmarc Casualty Insurance Company's ("Medmarc") Motion to Stay and its Motion to Quash the Subpoena Served Upon AIG Claims Services, Inc. ("AIG") or, in the Alternative, for a Protective Order. For the reasons stated below, Plaintiff's Motion to Stay is **GRANTED**. Plaintiff's Motion to Quash the Subpoena is **GRANTED** in part and **DENIED** in part. AIG must produce the reinsurance agreement between AIG and Medmarc applicable to the 1999-2000 policy of insurance issued by Medmarc to Arrow International, Inc. ("Arrow").

I. BACKGROUND

Defendant Arrow is the insured under an Excess Commercial General Liability policy issued by Medmarc. In an unrelated civil suit, an Arkansas state jury returned a verdict against Arrow, which included a punitive damages award of $4 million. Pursuant to the insurance policy, Medmarc defended Arrow in this Arkansas state suit. Thereafter, Medmarc filed a Complaint for Declaratory Judgment with this Court relating to the question of its responsibility to indemnify Arrow for the assessment of punitive damages. In the instant action, Medmarc requests that this Court declare the rights and liabilities of the parties as to insurance coverage for the punitive damages assessed against Arrow by declaring that coverage for punitive damages is precluded by the public policy of the Commonwealth of Pennsylvania. Apparently, it is Medmarc's position that a declaration by this Court that the public policy of Pennsylvania precludes coverage for punitive damages would relieve Medmarc from indemnifying Arrow for the punitive damages award assessed against it in the Arkansas litigation.

Arrow counterclaims seeking its own declaratory judgment that Medmarc has a duty to indemnify Arrow with respect to any amounts, including punitive damages, that it may become legally obligated to pay as damages in connection with the

Arkansas litigation. Arrow also brings a counterclaim for breach of contract and for attorneys fees.

Arrow served a subpoena on Medmarc's reinsurer, AIG, seeking certain information regarding any policies of reinsurance, including all drafts thereof, relating to the policies of direct insurance Medmarc issued to Arrow. Arrow also seeks all other communications between Medmarc and its reinsurer, AIG, potentially applicable to the policy of insurance issued by Medmarc to Arrow and relevant to the punitive damages claim assessed against Arrow. Medmarc brings the instant motion, objecting to the production of such reinsurance materials, asserting that the reinsurance information sought by Arrow is not relevant and/or contains privileged information not subject to discovery.

II. SCOPE OF DISCOVERY

Fed. R. Civ. P. 26(b)(1) authorizes discovery of relevant, nonprivileged matter that is reasonably calculated to lead to the discovery of admissible evidence. The rule provides in relevant part:

> Parties may obtain discovery regarding any matter, not privileged, which is relevant to the subject matter involved in the pending action, whether it relates to the claim or defense of the party seeking discovery or to the claim or defense of any other party, including the existence, description, nature, custody, condition, and location of any books, documents, or other tangible things and the identity and location of

> persons having knowledge of any discoverable matter. The information sought need not be admissible at the trial if the information sought appears reasonably calculated to lead to the discovery of admissible evidence.

Fed. R. Civ. P. 26(b)(1).

Fed. R. Evid. 401 defines "relevant evidence" as that which has "any tendency to make the existence of any fact that is of consequence to the determination of the action more probable or less probable than it would be without the evidence." Relevancy should be broadly construed at the discovery stage of litigation. See Oppenheimer Fund, Inc. v. Sanders, 437 U.S. 340, 351, 98 S. Ct. 2380, 57 L. Ed. 2d 253 (1978). It must be stressed that information inadmissible at trial is still discoverable if it is reasonably calculated to lead to the discovery of admissible evidence.

III. DISCUSSION

As an initial matter, Medmarc requests that the subpoena's enforcement by Arrow be stayed until such a time as the Court may rule on Medmarc's objections. This request is reasonable and will be GRANTED.

Medmarc first object to Arrow's attempt to discover the reinsurance materials on relevancy grounds, arguing that in declaratory relief actions involving an insurance coverage dispute, reinsurance information is irrelevant and only tenuously related to the issues of policy interpretation. Arrow counters,

stating that the reinsurance information it seeks from AIG is relevant to the interpretation of the punitive damages endorsement at issue. Arrow argues that because Medmarc consulted with AIG while evaluating its coverage position prior to denying coverage, that the reinsurance information may reflect Medmarc's intention as to indemnifying the underlying claim; may contain admissions regarding coverage; or may undermine Medmarc's current position on disallowing coverage for punitive damages.

An analysis of what reinsurance information is discoverable should distinguish between the reinsurance agreements themselves and other communications between cedents and their reinsurers. Federal courts have held that reinsurance agreements themselves are discoverable under Fed. R. Civ. P. 26, which mandates that a party provide other parties

> any insurance agreement under which any person carrying on an insurance business may be liable to satisfy part or all of a judgment which may be entered in the action or to indemnify or reimburse for payments made to satisfy the judgment.

Fed. R. Civ. P. 26(a)(1)(D); National Union Fire Ins. Co. v. Continental Illinois Corp., Nos. 85 C 7080, 85 C 7081, 1987 WL 11353, at *4-*5 (N.D. Ill. May 20, 1987); cf. Rhone-Poulenc Rorer, Inc. v. Home Indem. Co., 139 F.R.D. 609, 613 (E.D. Pa. 1991) (referred to herein as Rhone-Poulenc I).

In National Union Fire Ins. Co., the United States District Court for the Northern District of Illinois discussed at

some length the discoverability of reinsurance agreements in coverage litigation between a policyholder and its insurer. The court found that reinsurance agreements were discoverable under Rule 26 for the following reasons:

> Reinsurers ("person[s] carrying on an insurance business") are insurers' own insurers. If Insurers are held liable under the Policies, they will turn to their reinsurers for partial indemnification, as provided in the reinsurance agreements, for any "payments made to satisfy the judgment." Insurers contend their reinsurance agreements are not "insurance agreements" under Rule 26(b)(2).[1] True enough, reinsurance agreements are a special breed of insurance policy [actually, a contract of indemnity written by an insurer]. . . . But the English language remains the same: Reinsurers "carry[ ] on an insurance business" and "may be liable . . . to indemnify [Insurers] for payments made to satisfy the judgment" that Movants hope to obtain. Rule 26(b)(2) does not require that a party's insurer be directly liable to the other party. It is totally irrelevant that the reinsurers would pay Insurers and not the defendants and that Movants cannot directly sue the reinsurers.

In contrast, the United States District Court for the Eastern District of Pennsylvania in Rhone-Poulenc I found that reinsurance agreements were not per se discoverable under the federal rules. In that case, the court held that disclosure of reinsurance agreements is not required in cases in which the litigation between a policy holder and its insurer is limited to a request for a declaratory judgment and does not involve a claim for damages. See Rhone-Poulenc I, 139 F.R.D. at 613. Magistrate

1. Fed. R. Civ. P. 26(b)(2), prior to its 1993 amendment, addressed the discovery of insurance agreements.

Judge Edwin E. Naythons reasoned that in a declaratory judgment action, no money award is sought, thus, Fed. R. Civ. P. 26(b)(2) is not implicated because any ruling in the case would not require the insurer to be "liable to satisfy part or all of a judgment which may be entered in the action . . ." See also American Colloid Co. v. Old Republic Ins. Co., No. 93 C 0665, 1993 WL 222678 at *1 (N.D. Ill. June 21, 1993).

In this case, Medmarc seeks a declaratory judgment as to whether coverage for punitive damages is precluded by the public policy of the Commonwealth of Pennsylvania. Even if the rights and liabilities of the parties as to insurance coverage for punitive damages are definitively established by such a declaration, because of the nature of the action, this Court has not been asked by Plaintiff to enter a judgment ordering payment of such punitive damages for which Medmarc, and ultimately AIG, would be liable to satisfy. However, Arrow has brought a breach of contract counterclaim against Medmarc seeking indemnification for all punitive and compensatory damages assessed against Arrow in the Arkansas litigation. Therefore, because a money award is sought in the instant action, Fed. R. Civ. P. 26(a)(1)(D) mandates that AIG disclose the reinsurance agreement. The Court's Order will instruct AIG to produce only the final reinsurance agreement between AIG and Medmarc applicable to the

1999-2000 policy of insurance issued by Medmarc to Arrow. AIG will not be required to produce drafts thereof.

Apart from inspection of the reinsurance agreement itself, Arrow also seeks all communications between Medmarc and its reinsurer, AIG, involving the making and progress of the punitive damages claim at issue in the Arkansas state court action. The law with respect to communications between insurer and reinsurer is less clear. Given the number of different objections that may be opposed, the number of reasons asserted by the insured for desiring the information, and the variety of different issues that may exist in the action in which discovery is sought, there are decisions which have both allowed and denied this discovery. Whether communications between cedents and their reinsurers are discoverable appears to be dependent on the nature of the issues to which they are alleged to be relevant. Here, the policyholder, Arrow, asserts that the reinsurance materials are relevant to the interpretation of the punitive damages endorsement contained in its policy because Medmarc consulted with its reinsurer, AIG, while evaluating its coverage position prior to denying coverage.

Two decisions from the Eastern District of Pennsylvania in a dispute between Rhone-Poulenc and its insurers over coverage for underlying AIDS-related litigation illustrate the general principle that courts appear reluctant to permit discovery of

communications between cedents and their reinsurers for the purpose of establishing the proper interpretation of an unambiguous insurance policy, but are more willing to permit discovery for other purposes, such as defending against an insurer's effort to rescind a policy; to deny claims for late notice; to reconstruct a lost policy; or as extrinsic evidence of an ambiguous policy provision.

In Rhone-Poulenc I, 139 F.R.D. 609 (E.D. Pa. 1991), the court rejected the policy-holder's efforts to discover either the reinsurance agreements or communications with reinsurers for the purpose of interpreting the underlying policies. The court held:

> [D]iscovery concerning reinsurance agreements to which the plaintiffs were not parties would not assist in the determining of the mutual intent of the parties in the primary and excess insurance policies issued to the plaintiffs, which are in litigation in this case. Any information regarding reinsurance would at best be evidence of undisclosed unilateral intention, which would not be material to the interpretation of the insurance contract at issue.

Rhone-Poulenc I, 139 F.R.D. at 611-12 (internal quotations omitted).

The court did suggest, in dictum, that communications between an insurer and its reinsurer over the meaning of a particular policy provision could be discoverable only if there had been a previous determination by the court that the provision at issue was ambiguous and therefore subject to interpretation by

resort to extrinsic evidence. Rhone-Poulenc I, 139 F.R.D. at 612.

In Rhone-Poulenc II, Civ. A. No. 88-9752, 1991 WL 237636 (Nov. 7, 1991 E.D. Pa.), Judge Naythons reconsidered his earlier refusal to allow discovery of communications between the insurers and their reinsurers and granted such discovery. It is important to note that the court remained steadfast that the discovery was "irrelevant to determining the intent of the contracting parties," but it concluded that the discovery was relevant to the affirmative defenses of lack of notice and misrepresentation asserted by the insurers. With respect to the lack of notice defense, the court stated:

> By raising a defense, a party opens the door to the discovery concerning that defense. . . . Since whether or not the insurers gave timely notice to their reinsurers is clearly relevant to the notice defenses raised by many of the insurers, that information should be discoverable as to those insurers.

Rhone-Poulenc II, 1991 WL 237636 at *2.

In sum, the court in the Rhone-Poulenc cases took the position that reinsurance is, in many instances, discoverable for purposes of rebutting a defense, particularly of misrepresentation (as well as nondisclosure), lack of or late notice, or lost policy. However, reinsurance materials are irrelevant to determining the intent of the contracting parties or interpretation of an unambiguous insurance policy provision.

The only issue presented in the instant litigation is whether coverage is permitted for the punitive damages assessed against Arrow in the Arkansas litigation. This issue goes to the intent of the contracting parties and is a matter of insurance policy interpretation. There has been no allegation of ambiguity or request by the parties for a determination of ambiguity of the insurance policy at issue.[2] Therefore, in line with the Rhone-Poulenc cases, I believe that the reinsurance information is irrelevant and thus, not discoverable.

Even the cases cited by Arrow in support of discovery of reinsurance materials, where courts permitted discovery of reinsurance materials for purposes of interpreting the insurance policies at issue, are sufficiently analogous to the dictum found in the Rhone-Poulenc cases to lend support to the general principal that reinsurance materials are only potentially relevant when the issue of ambiguity has been raised. See Young v. Liberty Mut. Ins. Co., No. 3:96-CV-1189 (EBB), 1999 WL 301688 (Feb. 16, 1999 D. Conn.) (Providing broad latitude for discovery of evidence which might aid in interpreting the meaning of the terms of the subject insurance policies). Courts allowing discovery for purposes of policy interpretation reason that

2. Arrow asserts in its Answer, Affirmative Defenses and Counterclaims to Medmarc's Complaint that "[t]o the extent that the policy is ambiguous, any ambiguity must be construed against Plaintiff." While this is generally a correct statement of law, it does not sufficiently present an argument to the Court that the subject insurance policy is ambiguous.

reinsurance information may reflect the insurers' positions on the underlying claims and may also contain admissions regarding whether the claims were covered by their policies. However, in Young, the United States District Court for the District of Connecticut was initially asked to determine whether the insurance policies at issue were unambiguous, which would preclude the use of extrinsic evidence to vary or contradict the terms of the written policy. The Young court declined to rule on the ambiguity of the insurance policy at issue while discovery was still incomplete. Because the court left open the question of ambiguity, it did not prevent the plaintiffs from discovering evidence which may have presented an ambiguity in the insurance policies at issue or evidence which may have facilitated a full understanding of the meaning of the insurance policy's terms. Young, 1999 WL 301688 at *5. See also American Colloid Co., 1993 WL 222678 at *1 ("The rationale of Rhone does not apply if the extrinsic evidence can also be relevant to the initial determination of ambiguity.").

In the instant action, Plaintiff does not request a declaration that the insurance policy between Medmarc and Arrow is unambiguous nor does Arrow allege that the insurance policy at issue is ambiguous. Rather, Medmarc seeks a declaration as to Pennsylvania's public policy on coverage for punitive damages and how that public policy bears on the subject insurance policy.

Arrow has not explained why information shared between Medmarc and its reinsurer would shed light on the public policy of Pennsylvania as to coverage for punitive damages and how that determination affects the interpretation of the punitive damages provision in question.

Using the prior decisions as guidance, I believe that the reinsurance materials Arrow seeks from AIG are not relevant to the instant action. The punitive damage coverage provision at issue states "Except when prohibited by statute, coverage for Punitive or Exemplary Damages is included." Apparently, it is Medmarc's position that a declaration by this Court that the public policy of Pennsylvania precludes coverage for punitive damages would be the equivalent of an applicable statute prohibiting coverage for Arrow's claim for punitive damages. Arrow, however, maintains that it is entitled to payment for its claim for punitive damages assessed against it in the Arkansas state courts and at no time did Medmarc notify Arrow that it could not be insured for punitive damages because it was a Pennsylvania company.

It is true that communications between Medmarc and AIG regarding coverage for punitive damages have the potential to reveal opinions as to whether or not and on what basis coverage would be provided to Arrow. However, I fail to see why AIG's or Medmarc's opinions on these matters are relevant to the public

policy of Pennsylvania and how that public policy bears on the rights and liabilities of Medmarc and Arrow under their policy for direct insurance.

Pennsylvania law provides that the construction and interpretation of an insurance contract are governed by the parties' intent "as it is reasonably manifested by the language of their written contract." O'Brien Energy Sys. v. American Employers' Ins. Co., 427 Pa. Super. 456, 461, 629 A.2d 957, 960 (1993). Any opinion AIG formed or contributed with respect to Arrow's claim for punitive damages would have absolutely no bearing on the intent of the parties of the direct insurance relationship because AIG is not a party to their contract. Furthermore, any possible coverage position asserted by Medmarc to its reinsurer has little relevance in the context of an unambiguous policy provision. Medmarc and Arrow disagree as to whether Pennsylvania law or Arkansas law is applicable to the instant dispute, they are not contesting the meaning of the insurance policy provision at issue. Under these circumstances the reinsurance communications would be extrinsic evidence and would not lead to the discovery of admissible evidence.

For the reasons stated above, I find that the reinsurance communications sought by the subpoena irrelevant. With the exception of the actual agreement for reinsurance applicable to the 1999-2000 policy of insurance issued by Medmarc

to Arrow, AIG is not compelled to produce any other documents responsive to the subpoena served on it. Because I have disposed of Plaintiff's motion on relevancy grounds, its objections based on privilege will not be discussed.

An appropriate Order follows.

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MEDMARC CASUALTY INSURANCE COMPANY,	:	
Plaintiff,	:	CIVIL ACTION
v.	:	NO. 01-cv-2394
ARROW INTERNATIONAL, INC.,	:	
Defendant.	:	

ORDER

AND NOW, this 29th day of July, 2002, upon consideration of Plaintiff's Motion to Stay and Its Motion to Quash the Subpoena Served Upon AIG Claims Services, Inc. or, in the Alternative, for a Protective Order (Docket No. 13) and Defendant's response in opposition thereto (Docket No. 14), it is hereby **ORDERED** that Plaintiff's motion is **GRANTED** in part and **DENIED** in part.

1. Plaintiff's Motion to Stay in **GRANTED**.

2. AIG is **ORDERED** to produce the final reinsurance agreement between AIG and Medmarc applicable to the 1999-2000 policy of insurance issued by Medmarc to Arrow within five (5) days of the entry of this Order. AIG Claims Services, Inc. is not compelled to produce any other documents responsive to Defendant's subpoena served on it.

BY THE COURT:

RONALD L. BUCKWALTER, J.